352.043
G27g

NOV 28 1915

Reprinted from **The Annals** of the American Academy of Political and Social Science, Philadelphia, November, 1915.
Publication No. 950.

THE GERMAN MUNICIPAL BUDGET AND ITS RELATION TO THE GENERAL GOVERNMENT

By Karl F. Geiser,
Professor of Political Science, Oberlin College.

To a proper understanding of our subject it seems necessary to reverse the order suggested by the title and first explain the relation of the local to the general government. No attempt will be made to explain in detail the complicated relations of the German municipality to the various governmental units of administrative areas within the German Empire, though a complete study of the municipal budget would require it; for every taxpayer living within a rural or urban commune contributes directly or indirectly to several governmental organizations above the municipality. Obviously many of the sources of revenue of both the state and the imperial governments lie within the city. The income tax, for example, is a source of both state and municipal revenue, while the unearned increment tax, introduced into Frankfort in 1904, was adopted by the Imperial Government in 1911. It is now provided by law that this tax shall be collected and administered by the various states and the proceeds are to be divided between the imperial, state, and municipal treasuries. In practice, however, this tax is collected by the municipal authorities who may, by sanction of the state, levy a supplemental unearned increment tax not to exceed 100 per cent of the imperial tax. I mention these facts here merely to show the complicated financial relations between the local and general governments that we may better appreciate the problems presented to the budget makers.

Before entering upon details, other facts of a general nature should also be kept in mind. In considering German municipal practices it should be remembered that the German Empire is composed of twenty-six more or less independent states, that each of these states has its own legislative body, its own administrative officials, its own political subdivisions and its own system of local government. A mere glance at the history of Germany—its former

P 39098

numerous petty states, its local customs, its independent cities, its leagues and confederations and its comparatively recent Empire —will enable us to understand why there are still differences in the administration of local affairs in different parts of the Empire. The administration of finance forms no exception to this general statement. Whatever may be said, therefore, concerning the policy of one state should not necessarily be assumed to apply to all states. However, it should be observed in this connection that there is coming to be more and more uniformity, in the administration of local matters, through the influence of the central government, through national municipal congresses, through numerous journals devoted to local government and through the readiness of one state to adopt a superior system that has proved successful in another state.

Since Prussia comprises about three-fifths of the area of the Empire and contains, in round numbers, 40,000,000 of the Empire's total population of 65,000,000, we may properly regard that state as not only dominant in the Empire but as typical of German local administration. At the same time, against the tendencies toward local uniformity through the forces mentioned, especially through the dominance of Prussia, must be placed the fact—the most cardinal fact of local finance—that there is a wide latitude of local autonomy. The German city is a city of general, not delegated powers and may do everything not specifically denied it by the state or the imperial government. This fact operates against uniformity. But whatever degree of difference or uniformity exists, from the standpoint of the individual the municipal budget must take into account the fact that every taxpayer within the municipality must or may contribute in some form, directly or indirectly, to the following governmental or administrative organizations: (1) The Empire, (2) the State, (3) the Province, (4) the Government District, a subdivision of the province, (5) the Circle and (6) the Commune, of which there are two kinds—rural and urban.

From first to last, each one of these jurisdictions,—whether organized for purposes of general or local government, whether a subdivision of a larger government used for purely administrative purposes or a government largely independent in itself, such as a city—has a set of administrative officials, assistants, clerks, and employees, some of whom, in connection with their general

work of administration, are also specially organized for the administration of finance. While the finance administration of both the Empire and of the state is carried on by a division of the respective ministries of finance and charged with only financial matters, there is in the cities no special municipal budget commission or board of estimate. Every phase of budget making is in the hands of the regularly constituted city officials. A word should, therefore, be said concerning the general city organization. This consists of two general organs of government. First, there is the council, elected by a popular vote, a body with functions similar to those of an American municipal council. The second organ of city government is an administrative board, at the head of which stands the bürgermeister or mayor. This board, called the magistrat, acting in a collective capacity controls and directs the city government; but the individual members also serve as heads of departments and in various other capacities. They are elected by the council, the number being usually one-fourth to one-third of that of the council.

The magistrat prepares the business for the council, and supervises municipal enterprises; it has custody of the revenues and documents; it cares for the civic property, appoints employes, represents the municipality as a corporation and acts as an agent for the state and imperial governments in matters assigned to them by law or by the higher officials. Among the most important duties thus assigned are those pertaining to finance. Certain forms of taxation are of course classed as federal taxes, such as imposts and excises, the latter including postage stamps, bill-stamps, the inheritance tax, a tax upon spirits, beer, tobacco, sugar, and salt. The collection and administration of these taxes come entirely within the jurisdiction of the federal government but in practice many of them are levied by means of the state and local authorities, and in some instances the general government divides a portion of these revenues with the state or with the state and municipality, as in the case of the unearned increment tax, already noted, which, by the way, is both an imperial and a municipal tax.

As in America, there is a growing tendency in Germany, on the part of the general government, to encroach upon the original sources of state and municipal revenue. The inheritance tax is a good example of this tendency. As the unearned increment tax,

though first used in one of the German colonies, was first used on the continent in Frankfort where its successful operation suggested itself as also a convenient source of federal revenue, so the inheritance tax was first a Prussian tax being provided by an elaborate law of that state in 1891. In 1906, in connection with a movement for the reform of imperial finance, the Prussian law was incorporated into a federal statute and the inheritance tax became a federal tax with the provision, however, that one-fourth of the gross receipts from this source should be turned over to the various states. Such changes in the sources of revenues obviously necessitated the combination of national, state and local functions and the mutual administration of finance is a natural consequence. It should not, however, be assumed that the encroachment of the general government upon the field of local finance has seriously crippled the municipalities, for they have been quite free to adopt new methods and they have readily found new sources of income. The high order of German municipal statesmanship and the wide latitude of local autonomy have furnished the motive and the occasion to solve the problems involved.

Having considered some of the relations between general and local finance, we may, it is hoped with a better understanding, consider some of the chief features of the municipal budget in particular.

While the laws of Prussia permit a city to plan its budget for one, two or three years, the yearly budget is the rule, the financial year beginning April 1, and ending March 31. The leading facts in budgetary procedure are as follows: From the reports and estimates of revenues and expenditures presented to it by the various administrative departments, the magistrat, *i. e.*, the administrative board, already described, makes an annual estimate not later than January 1 preceding the fiscal year. This estimate must be published for public examination and criticism for a period of eight days after which it is formally presented to the city council whose approval is necessary before it becomes the established budget. At the time of the preliminary estimate a copy is sent to the authorities superior to the municipality. Their "sanction," however, which the law requires, is not necessary unless new taxes are imposed or old ones changed. If there is no objection by the superior authorities and the city council approves it, the estimates thus

finally established become the budget for the fiscal year following. In a word it becomes the financial law of the municipality and, after its final approval, it becomes the duty of the magistrat to see that all officials having any connection with its administration strictly adhere to the prescribed budget. Special budgets may, however, at any time be presented if unforseen events arise to demand it; but this is seldom the case. When it is necessary, however, the procedure followed is the same as that of the regular budget. The mere fact, however, that a special budget is permitted by law is more important to us than its details, for it suggests one of the most cardinal principles of local finance as well as of local government—the freedom allowed by the state to cities in the management of their local affairs.

The form and details of a municipal budget are not prescribed by general law; that is left to the local officials, yet certain general and well defined practices, common to all budgets, enable us to set forth their main features. It may be added in this connection that there are numerous standard works dealing with municipal budget-making that have done much to unify their form and content.[1] Municipal tax congresses and frequent recommendations and suggestions from the ministries of the interior and of finance also tend toward local uniformity.

The municipal budget (Haushaltsetat) is made up of two general classes of minor or subsidiary budgets, viz., (1) budgets which affect taxation, *i. e.*, either increase or decrease it; and (2) budgets which do not, such as savings bank-budgets, foundation-budgets, etc. Each of these general classes is again divided into two heads, comprising (a) *ordinary administration* (Ordentliche Verwaltung) and (b) *extraordinary administration* (Ausserordentliche Verwaltung); then follow, as occasion demands, the minor subdivisions or special items of administration whence the original or primary estimates are made; that is to say, the needs of the ultimate administrative divisions must be known to the makers of the general budget before it is drafted. In the order of presentation, however, the general budget precedes the separate estimates. It assigns to the various departments and administrative subdivisions the amount

[1] An excellent work upon this subject is A. Machowicz, *Grundsätze für das Etats-, Kassen-, Rechnungs-, Revisions- und Anleihewesen der Stadtgemeinden.* Dritte Auflage. Berlin, 1908.

which in the judgment of the magistrat may be expended during the following year. The general budget merely contains the results of the estimates of the separate departments, which estimates must be independently approved by the magistrat and council. The *ordinary* part of the budget includes the regular current incomes from communal property, the portion granted to the municipality by the state, province and circle; it also includes taxes and exemptions, dues, fees and miscellaneous contributions. The *extraordinary* part includes incomes from exceptional or special sources, as gifts, legacies, sales from land and loans. The divisions of a general budget as illustrated by Machowicz[2] are as in table on page 7.

Each of the divisions is again subdivided under the general headings of "Income" and "Expenditures" into minor divisions and items, and, needless to say, in an orderly manner, with references and cross-reference to audits, approvals and vouchers, until the minutest detail of revenue and expenditure is traced to its original or ultimate source.

While there is no state audit of local finance in Germany, as in some of our American states, there is little danger of mismanagement of funds, since a "revision" of the local treasury is made by the executive every month, on specified days, notice of which is given to the council beforehand so that it may appoint members to be present; and at least once a year there is a surprise "revision" of which no notice is given, at which either the chairman of the council or a member appointed by that body must be present. Further control of the budget is provided by requiring the magistrat to keep and publish a register (Lagerbuch) of the municipal property, both real and personal. This register, which is open to public inspection, is periodically revised and must be so prepared as to present a clear account of the tangible municipal assets.[3]

It would be impossible to place within the limits of this paper a comprehensive outline of the various sources of municipal revenues, since German cities are quite free to choose not only the kind of tax but also the objects of taxation. I will, therefore, confine my remarks upon this phase of the subject to a limited number of observations and to a summary of general results.

[2] P. 141.

[3] W. H. Dawson, *Municipal Life and Government in Germany*, 1914, pp. 344–45. This work contains the best account in English of German municipal finance.

Principal Budget for 1907

Income											Expenditure											
Estimate for				Compared with 1906				No. of B.	Description of subsidiary budgets		Estimate for				Compared with 1906				Budget of 1907 closes			
1907		1906		Incr.		Decr.					1907		1906		Incr.		Decr.		Bal.		Addit'n	
M.	Pf.	M.	Pf.	M.	Pf.	M.	Pf.				M.	Pf.	M.	Pf.	M.	Pf.	M.	Pf.	M.	Pf.	M.	Pf.
									A. Ordinary Administration													
								2	General administration													
								3	Administration of estate													
								4	Buildings													
								5	Schools													
								6	Poor													
								7	Augusta Victoria Hospital													
								8	Disinfection													
								9	Welfare													
								10	Public baths													
								11	Public library and reading room													
								12	Fire department													
								13	Trade and traffic													
								14	Improvement													
								15	Cemeteries													
								16	Foundations													
								17	Capital and debts													
								18	Taxes													
									Total.....													
									B. Extraordinary Administration													
								19	Revenues and expenditures													
									Total.....													

Schöneberg.....190 .

.....Magistrat.....

The Prussian municipal ordinance of 1853 made no provision for limiting cities either in the rate or the objects of taxation. But a law of July 14, 1893, amended the former law by providing that taxes could only be imposed in so far as the revenues from city property, plus state grants, did not provide an income sufficient to meet the expenses of government. In general it may be said that the restrictions by the general government upon local finance administration are all indirect, suggesting means of avoiding excessive taxation and accumulation of debt rather than preventing the carrying on of communal enterprises and undertakings. Thus, for example, in 1907 the Prussian ministers of finance and of the interior issued a joint rescript commanding rural and urban authorities to redeem loans at a higher rate than had been the custom. The rate for the redemption of general loans was increased from 1 per cent to $1\frac{1}{4}$ per cent; loans for streets and similar work were now to be redeemed at $2\frac{1}{2}$ per cent and sewerage loans at 2 per cent. In 1912 another rescript advised greater caution on the part of the state authorities in sanctioning loans. To meet extra expenditures the general government also advised municipalities to establish emergency and new building funds; and Düsseldorf has for some time set aside an annual amount for a fund for new buildings; Cologne and other cities do the same. The superior authorities have also ordered one-third of the cost of new buildings to be defrayed otherwise than by loans. This restriction, it should be noted, applies only to expenditures for non-productive purposes; there are no objections on the part of the central authorities to establishing land-purchase funds by means of initial loans; nor are there any general restrictions upon the local tax rates, such, for example, as we have in some of our American states, which prevent cities from meeting the necessary expenses of government or from reaching out into new activities which would really benefit the whole community. In a word, the state says to a city, in effect:

Develop your own sources of revenue, but tax your citizens as little as possible; you may engage freely in any kind of enterprise you please, providing you make these enterprises pay their own expenses and, in some instances, even pay a profit;[4] we shall be glad to advise you, but we trust you to govern yourselves well.

[4] The Prussian law of communal taxation makes a distinction between enterprises which may be carried on for gain and those which are described as *Anstalten* or "communal institutions" which are to benefit the whole public and are not intended primarily for profit.

This attitude of the state toward the local community throws the responsibility for efficient management upon the city, and, therefore, with the consciousness that its destiny is in its own hands, the city develops a high order of municipal statesmanship. Officials are chosen for their respective positions, not because they belong to a particular party, but for the same reason that American private corporations choose their officials, namely, efficiency. Indeed this is the chief explanation of why German public corporations and American private corporations are both successful. It would however be unjust to many American cities not to acknowledge in extenuation of mismanagement the fact of ill-advised and often unjust state interference, for no man can serve two masters. This interference on the part of the American state, of course, prevents the use of many profitable sources of income. Our short tenure of service also prevents our officials from planning a continuous, long-sighted municipal policy.

What this freedom from state interference means to a German city may be shown by a few examples. The present mayor of Ulm has held his position for a quarter of a century. When he entered upon the duties of office he advocated the purchase of land to carry forward an extensive housing policy, and during his administration about 1,500 acres of land have been added to the corporate wealth at an expense of $2,650,000. Of this amount 500 acres have been sold at a price exceeding the total cost of all lands purchased, thus leaving 1,000 acres free of debt which are now yielding a net revenue of $18,750 annually.[5] Here was a colossal undertaking which, instead of being a burden upon the city, has been its chief source of revenue. A similar example of municipal enterprise, though rather unusual in its results, is furnished by the little town of Klingenberg in Bavaria. It has a population of only 2,000, yet it owns forest, and other lands including a clay pit, from which it pays, not only all expenses of government, but also an annual cash bonus to its freemen. During a recent fiscal year, after paying all expenses of government and adding $500,000, to its reserve fund, it presented a cash dividend of $100 to every freeman. It would be a mistake, however, to suppose that German municipalities are, as a rule, free from debt; the illustration, just mentioned, has been given rather to suggest the freedom with which German cities may engage

[5] This statement applied to year 1912.

in profitable enterprises and thus relieve their budgets of excessive tax rates. As a matter of fact German cities have, as a rule, a large debt and the cost of government is, as in America, on the increase, owing in part to the high cost of living and in part to the large number of public enterprises and undertakings which in America would be in private hands. Thus the rural and communal debt in the Empire in 1907 was $26.50 per capita, while in 1910, the debt of eighty-four of the largest cities of the Empire, representing a population of fifteen and a half millions, was $74.25 per capita. But a large portion of this debt represents an outlay of capital engaged in profitable enterprises, and is therefore an actual surplus, a net gain to the municipality.

The relation of public enterprises to the German municipal budget, it will thus be seen, is an important one; in fact it constitutes the chief problem in budget making and I have given it special consideration because it is the distinguishing feature which differentiates a German municipal budget from an American municipal budget. What it means to the total revenues of a German city, and incidentally to taxation, may best be seen by comparing the incomes of the various sources of revenues with the expenditures for their cost, maintenance and administration. This comparison applies to all German cities and rural communes having a population of over 10,000, and is based upon a report of the imperial government made in 1907 and published in 1908.

Of the total gross revenue 33.2 per cent came from taxation, 25.9 per cent from communal enterprises and undertakings of all kinds, 5.9 per cent from the administration of communal estates and investments, 5.1 per cent from educational and art institutions, 3 per cent on account of poor relief, orphans and hospitals, 4.7 per cent from the building administration, and the remainder, 22.2 per cent, from the general, police and other branches of administration.

Of the gross expenditures, 23 per cent were for the administration of communal enterprises and undertakings, 17.4 per cent for educational and art institutions, 14.3 per cent for the administration of debts, 11.8 per cent for general and police administration, 9.9 per cent for building administration, 7.6 per cent for the administration of charities and hospitals, and the remainder, 16 per cent, for miscellaneous branches of administration.[6]

[6] These results are quoted from Dawson, pp. 341–342.

Limitations of space forbid an analysis and discussion of the various sources of revenue and the final distribution of that revenue, the results of which are summarized on page 10. It will be noted that of all of the sources of income mentioned, that from taxation yields almost exactly one-third of the total. The various forms of taxation, both direct and indirect, their history and application to budget making, form an instructive study in municipal finance. But I am compelled to content myself by appending two tables showing the kinds of direct and indirect taxes, the total income from each of these in various classes of cities grouped according to population, the per capita income from each group, and the percentage each group bears to the total of the total income from each source. These tables apply to Prussian cities and are taken from the *Kommunales Jahrbuch*[7] of 1913–14:

INCOME FROM DIRECT MUNICIPAL TAXES IN PRUSSIA REPORTED MARCH 31, 1912

Class of cities having a population	Total income		Percentage of total income from each source			
	Aggregate	Per capita	Income tax	Real estate tax	Trade tax	
Berlin	$22,587,500	$11.10	51.8	31.8	16.0	0.3
Above 200,000 (excl. of Berlin)	41,410,000	9.225	61.1	27.1	11.4	0.4
From 100,000–200,000	23,360,000	8.85	60.4	27.9	11.3	0.5
From 50,000–100,000	15,687,500	7.35	60.3	25.6	13.7	0.5
From 25,000–50,000	12,797,500	6.60	61.4	25.5	12.6	0.5
From 10,000–25,000	15,215,000	6.025	62.1	24.6	12.9	0.4
From 7,000–10,000	3,657,500	4.725	60.2	26.9	12.3	0.6
From 5,000–7,000	3,382,500	4.45	57.8	29.0	12.6	0.6
From 3,000–5,000	4,017,500	4.20	56.3	30.4	12.6	0.8
From 2,000–3,000	2,170,000	3.65	53.1	33.7	12.3	0.9
Less than 2,000	1,160,000	2.90	51.5	36.0	11.3	1.2
Total	$145,450,000	$7.55	59.1	27.7	12.7	0.5

[7] In translating the German "Mark" into the American denominatoin I have, for convenience, called the Mark equivalent to 25 cents; it is a little less.

3 0112 061909732

INCOME FROM INDIRECT MUNICIPAL TAXES IN PRUSSIA REPORTED MARCH 31, 1912

Class of cities having a population	Total income		Percentage of total income from each source						
	Aggregate	Per capita	Conveyance tax	Unearned increment tax	Retail liquor licences	Beer brew and distillation tax	Amusement tax	Dog tax	Miscellaneous taxes
Berlin	$2,112,500	$1.05	52.1	25.4	—	8.6	—	13.9	—
Above 200,000 (excl. of Berlin)	5,217,500	1.175	44.5	18.4	2.2	10.4	15.4	7.3	1.8
From 100,000–200,000	2,760,000	1.05	39.9	15.6	5.1	14.1	13.3	8.3	3.6
From 50,000–100,000	1,630,000	.775	35.2	14.9	5.5	18.9	15.0	9.4	1.1
From 25,000–50,000	1,132,500	.575	37.3	14.2	4.8	16.3	15.2	10.8	1.2
From 10,000–25,000	1,177,500	.475	36.7	8.5	2.1	22.9	16.1	12.3	1.4
From 7,000–10,000	300,000	.40	41.1	9.9	1.0	20.9	12.3	12.9	1.9
From 5,000–7,000	252,000	.325	43.3	3.6	0.9	22.7	13.6	14.7	1.2
From 3,000–5,000	320,000	.325	41.9	5.7	1.1	24.3	11.9	13.0	2.1
From 2,000–3,000	190,000	.325	47.1	5.0	1.0	20.7	11.5	12.7	2.0
Less than 2,000	102,500	.25	44.0	3.2	0.6	22.9	11.6	14.0	4.2
Total	$15,197,500	$0.80	42.5	16.3	2.9	14.1	12.6	9.7	1.7